326 U.S.
ARG-ASH

SEP 18 19
CHARLES ELMORE CR
OL

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

D

No. 436

M. M. ARGO,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

H. Cecil Kilpatrick,
Douglas Arant,
Counsel for Petitioner.

Mills & Kilpatrick,
Washington, D. C.;
Ellene Winn,
Virginia Lloyd Dunlap,
Bradley, Baldwin, All & White,
Birmingham, Alabama,
Of Counsel.

INDEX

Subject Index

	Page
Petition for writ of certiorari	1
Summary statement of the matter involved	1
Questions presented	6
Reasons relied upon for allowance of the writ	8
Brief in support of petition	11
I. Opinions of the courts below	11
II. Jurisdiction	12
III. Statement of the case	12
IV. Specifications of errors	16
V. Argument	18
Summary of the argument	18
Point A—The judgment of the District Court in the case of *Argo* v. *Willingham* is *res adjudicata* and operates as an estoppel to raise the issues there adjudicated which are material in the case involving the year 1940	21
Point B—The judgment of the District Court in the case of *Argo* v. *Willingham* should have been given weight by the Tax Court in its consideration of the case involving the years 1938 and 1939.	32
Point C—The decision of the Tax Court that Birmingham Electric & Manufacturing Company was not a bona fide partnership for income tax purposes for the years 1938, 1939 and 1940 was not supported by substantial evidence	34
Appendix	38

Table of Cases Cited

Argo v. *Willingham*, Collector of Internal Revenue	2
Bates v. *Bodie* (*1918*), 245 U. S. 520, 62 L. Ed. 444, 38 Sup. Ct. 182	19,26
Bennett v. *Commissioner of Internal Revenue* (C. C. A., 5th 1940) 113 F. (2d) 837, 130 A. L. R. 369	19'29

152178

Page

Bishop v. *Smith*, 9 Kan. App. 602, 58 Pac. 493..... 19,32
Commissioner v. *American Seating Co.*, (1931) 50 F. (2d) 681..... 19,30
Coulson v. *Scott* (1910) 167 Ala. 606, 52 So. 436..... 20,34
Deposit Bank of Frankfort v. *Board of Councilmen* (1903) 191 U. S. 499, 48 L. Ed. 276, 24 Sup. Ct. 154. 19,28
Donald v. *White Lumber Co.*, (C. C. A., 5th 1934) 68 F. (2d) 441..... 19,28
Dutton v. *Woodman*, 9 Cush. (Mass.) 255..... 19,32
Guin v. *Grosselli Chemical Co.*, (1916) 197 Ala. 117, 72 So. 413..... 19,32
Hayes v. *Gudykunst*, 11 Pa. 221..... 19,32
Helvering v. *Kehoe*, (1940) 309 U. S. 277, 84 L. Ed. 751, 60 Sup. Ct. 549..... 20,34
Helvering v. *Rankin*, (1934) 295 U. S. 123, 79 L. Ed. 1343, 55 Sup. Ct. 732..... 20,34
Johnson Co. v. *Wharton*, (1894) 152 U. S. 252, 38 L. Ed. 429, 14 Sup. Ct. 608..... 19,28
Kimmerle v. *Lowitz*, 203 Mich. 482..... 19,32
Last Chance Mining Co. v. *Tyler Mining Co.*, (1894) 157 U. S. 683, 39 L. Ed. 859, 15 Sup. Ct. 733..... 19,27
Leininger v. *Commissioner*, (1934) 29 B. T. A. 874, affirmed (C. C. A., 6th 1936) 86 F. (2d) 791..... 8,19,22
Mary Haller, (1932) 26 B. T. A. 395 (affirmed 68 F. (2d) 780)..... 19,28
Mayer v. *Kornegay*, (1907) 152 Ala. 650, 44 So. 839... 19,32
McDonald v. *Hannah*, (Circ. Wash. 1892) 51 F. 73.... 20,34
N. L. R. B. v. *Columbian E. & S. Co.*, (1939) 306 U. S. 292, 83 L. Ed. 660, 59 Sup. Ct. 501..... 20,34
N. L. R. B. v. *Thompson Products*, (C. C. A., 6th 1938) 97 F. (2d) 13..... 20,35
New Orleans v. *Citizens Bank of Louisiana*, (1897) 167 U. S. 371, 42 L. Ed. 202, 17 Sup. Ct. 905..... 19,28
Southern Pacific Railroad Co. v. *United States*, (1897) 168 U. S. 1, 42 L. Ed. 355, 18 Sup. Ct. 18..... 18,21
Tait v. *Western Maryland Railroad Co.*, (1933) 289 U. S. 620, 53 Sup. Ct. 706, 77 L. Ed. 1405..... 18,22,27
Toy v. *Gong*, (1918) 87 Ore. 454, 170 Pac. 936..... 19,32
United States v. *Nunnally Investment Co.*, (1942) 316 U. S. 258, 86 L. Ed. 1455, 62 Sup. Ct. 1064..... 32

Page

Wilmington Trust Co. v. *Helvering*, (1942) 316 U. S. 164, 86 L. Ed. 1352, 62 Sup. Ct. 984 20,34
Wood v. *Byington*, 2 Barb. Ch. (N. Y.) 387 19,32

TEXTBOOKS

34 Corpus Juris, *Judgments*, Sec. 1313 19,31
34 Corpus Juris, *Judgments*, Sec. 1508 20,33
Federal Rules of Civil Procedure, Rule 16 .....
2 Freeman on Judgments (5th Ed.) Sections 712, 900 et seq., 904 19,32
"Taxes" (magazine), August, 1945. Article by Robert J. Bird on "Res Judicata" .....

STATUTE

Internal Revenue Code, Section 3772 (d) 4,21,38

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 436

M. M. ARGO,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT.

MAY IT PLEASE THE COURT:

The petition of M. M. Argo respectfully shows to this Honorable Court:

Summary Statement of the Matter Involved

The controversy involves petitioner's federal income tax liability for the years 1938, 1939, and 1940. Petitions for review of two decisions of the Tax Court of the United States (one involving the years 1938 and 1939, and one involving the year 1940) were consolidated for hearing in the Circuit Court of Appeals. (Tr. p. 104)

Birmingham Electric & Manufacturing Company, an Alabama corporation, all of the capital stock of which was owned by the petitioner, was dissolved on December 31, 1936. Petitioner thereupon entered into an oral agreement of partnership with his wife and his three minor children, whereby each of them became a partner owning a one-fifth interest in a partnership which was to carry on the business formerly conducted by the corporation. During 1937 and during the tax years here involved—1938, 1939, and 1940—Birmingham Electric & Manufacturing Company (sometimes hereinafter referred to as the "company"), which was formed pursuant to this partnership agreement, engaged in the business of rebuilding and repairing electrical equipment and of selling such equipment. (Tr. pp. 50-51)

The Collector of Internal Revenue for the District of Alabama assessed against the petitioner a deficiency of $876.14 for the year 1937 on the ground that no bona fide partnership existed and that petitioner was subject to income tax on the entire net income of the company. After paying the assessment, the petitioner sued the Collector in the United States District Court for the Northern District of Alabama to recover the amount thus paid. The case, which was entitled *Argo* v. *Willingham, Collector of Internal Revenue,* was tried by the Court and a jury. It was stipulated by the parties at the trial that, if the jury found that there was a bona fide partnership between the petitioner, his wife, and three children during the calendar year 1937, the issues should be adjudged in favor of the petitioner. The jury found that such a partnership existed during the year 1937 and the Court thereupon, on October 16, 1942, entered judgment for the petitioner. The Collector appealed to the Circuit Court of Appeals, but later dismissed his appeal. (Tr. pp. 94, 141-152)

For the years here involved (1938, 1939, and 1940), the Commissioner again taxed the petitioner on the entire income from the partnership, asserting the same ground as the basis for his action. The petitioner appealed to the United States Board of Tax Appeals (which thereafter became the Tax Court of the United States). The petition for review as to tax liability for the years 1938 and 1939 was filed with the Board of Tax Appeals on February 21, 1942; the petition as to liability for the year 1940 was filed on August 24, 1942. The petitioner made the same contentions in the Tax Court that he had made in the former case in the District Court and asserted in addition that the judgment of the District Court was *res adjudicata* of and operated as an estoppel against the Commissioner to raise *the same issues and questions* with respect to the years 1938, 1939, and 1940 that had been raised and adjudicated with respect to the year 1937. The pleadings and the Order on Pre-trial Hearing which formulated the issues in accordance with Rule 16 of the Federal Rules of Civil Procedure, and Judgment of the District Court in the former case were introduced in evidence in the Tax Court. (Tr. pp. 141-152)

The evidence before the Tax Court showed without dispute that from the date of its formation on January 1, 1937, until the end of 1940—a period including *the year 1937,* with respect to which the said judgment was rendered in the District Court, and *the years 1938, 1939, 1940,* tax liability for which is here in question—the company continued to operate in the same manner; that the nature of its business—rebuilding and repair of electrical equipment and sale of such equipment—remained the same throughout the years 1937, 1938, 1939, and 1940; that during that period, the petitioner's work and activities in the business remained the same; that the activities of the other partners in the business also remained the same, except

that the activities of three of the other partners—petitioner's wife and his two older children—were greater in 1938, 1939, and 1940 than in 1937; that the number of persons (other than the partners) employed by the company remained approximately the same (from 25 to 30) during those four years; and that the percentage of return on the company's investment was smaller in the years 1938, 1939, and 1940, than in the year 1937.

The Tax Court recognized the effect of the former judgment, saying in its opinion:

> "* * * the verdict of the jury and the judgment entered thereon involved a determination that there was a partnership for Federal income tax purposes in 1937. The question presented here in docket No. 112248 is the same except for different years, such question requiring a determination of whether there was a partnership for Federal Income tax purposes between the same persons in the same business during the year 1940" (R. p. 86).

The Tax Court held, nevertheless, as to the years 1938 and 1939, that the parties were not the same or in privity, and that accordingly the principle of *res adjudicata* or estoppel by judgment was not applicable; and, as to the year 1940 (the parties being the same or in privity by virtue of section 3772(d) of the Internal Revenue Code), that the principle was inapplicable, because the evidence which was submitted to the jury in the trial in the District Court was not in the record before the Tax Court.

The Tax Court declined to give any weight to the former judgment in its consideration of petitioner's tax liability for the years 1938, 1939 and 1940; and in effect held that, in spite of the decision of the District Court that a partnership for income tax purposes existed throughout the year 1937, the burden remained on petitioner to prove that such a partnership existed in 1938, 1939 and 1940; and

that the facts adjudicated by the former decision—including the formation of a bona fide partnership for income tax purposes on January 1, 1937, and the ownership by each partner of a one-fifth interest in such a partnership throughout the year 1937—were neither conclusively nor presumptively true and that these issues, so far as material in the cases involving the later years, could again be inquired into without reference to the former decision.

The Tax Court held further that, although the evidence before it afforded "no basis for a positive finding that the activities and services of the petitioner were the main factors in the production of the income" of the company, it pointed "quite strongly in that direction"; that the petitioner had failed to show affirmatively that his activities and services were not the main factors in the production of such income; and that, accordingly, the petitioner was taxable upon the entire net income of the partnership.

The Tax Court's conclusion that petitioner failed to show that his activities and services were not the main factors in the production of the company's income was based on two subsidiary findings of fact or statements of fact, which are set forth and stressed in that court's opinion: (1) the statement that the court had not been "informed as to whether other persons were employed" by the company (R. p. 89) and (2) the statement that the annual earnings of the company during the years 1937-1940, inclusive, were "50 per cent and more in excess of the capital investment in physical assets" (R. p. 90). The record shows that the company had an average of from 25 to 30 employees during the years in question (See Respondent's Exhibits H-M, Certified in original form); and that the company's investment consisted not only in the physical assets shown by the balance sheets at the beginning of each year, but in large items of cash expended annually

for labor, material, etc., and that the return on the company's total investment did not exceed 10% in either 1938, 1939, or 1940.

In the judgment review of which is here sought, the Circuit Court of Appeals for the Fifth Circuit affirmed the judgments of the Tax Court.

Questions Presented

(1) Whether and to what extent the judgment of the United States District Court for the Southern Division of the Northern District entered on October 16, 1942, in the case of *Argo* v. *Willingham* constitutes *res adjudicata* or operates as an estoppel by judgment in the suit with respect to petitioner's income tax liability for 1940.

(a) Whether the following issues, which were determined by the former judgment, are material to a determination of the questions raised in the suit involving the year 1940:

> (1) The taxpayer on January 1, 1937, made valid bona fide gifts to members of his family of their several interests in the business.
>
> (2) The taxpayer on January 1, 1937, ceased to be the individual owner of the business and the several partners became the owners thereof.
>
> (3) A partnership valid for income tax purposes was *formed* January 1, 1937, and existed throughout that year.

(b) If the three issues set forth in (a) are material to a determination of the issues in the suit involving the year 1940, whether the respondent is estopped to controvert the former adjudication as to those three issues, regardless of whether the evidence upon which the former adjudication was based appears in the record of the instant case.

(c) Whether the adjudication in *Argo* v. *Willingham* that a partnership valid for income tax purposes existed throughout the year 1937 estops the respondent from asserting that no such partnership existed in 1940, when, according to the undisputed evidence in the instant case, the business was conducted in the same fashion without substantial change of any kind from January 1, 1937, through the year 1940.

(d) Whether the said adjudication operates as *res adjudicata* or as an estoppel by judgment in the circumstances set forth in (c), regardless of whether the evidence upon which the former adjudication was based appears in the record of the instant case.

(2) Whether the partnership determined by the former judgment to have been in existence for income tax purposes during 1937 is presumed, in the absence of proof, to continue to exist and to conduct its operations in the same manner.

(3) Whether the respondent has the burden of proving discontinuance of the partnership existence of which, for income tax purposes, throughout the year 1937 has been determined by the former judgment.

(4) Whether the Circuit Court of Appeals erred in failing to hold that the Tax Court, in its consideration of the case involving the years 1938 and 1939, should have given weight to the former judgment of the District Court.

(5) Whether the Circuit Court of Appeals erred in failing to hold that the partnership was a valid and bona fide partnership for income tax purposes during the years 1938, 1939, and 1940.

(6) Whether the Circuit Court of Appeals erred in holding that the findings of the Tax Court were supported by substantial evidence.

(7) Whether a decision by the Tax Court of the United States which is based upon primary or subsidiary findings of fact contrary to the undisputed evidence is a decision in accordance with law.

Reasons Relied Upon for Allowance of the Writ

The decision rendered in this case by the Circuit Court of Appeals for the Fifth Circuit is in conflict with the decision of the Circuit Court of Appeals for the Sixth Circuit in the case of *Leininger* v. *Commissioner* (1936), 86 Fed. (2d) 791.

With respect to the applicability of the principle of *res adjudicata* or estoppel by judgment in the case involving the year 1940, the Circuit Court of Appeals for the Fifth Circuit has decided an important question of federal law in a way which is not in accord with the applicable decisions of this Court.

Insofar as the decision of the Court below holds that the Tax Court did not err in failing, in its consideration of the case involving the years 1938 and 1939, to give weight to the judgment of the District Court it decides an important question of federal law which has not been but which should be decided by this Court.

Insofar as the decision of the Court below holds that the decision of the Tax Court was supported by substantial evidence, it decides important questions of federal law respecting the validity of partnerships for income tax purposes which have not been but which should be decided by this Court.

Insofar as the decision of the Court below holds that the decision of the Tax Court was supported by substantial evidence, it decides an important question of federal law in a way probably not in accord with the applicable decisions

of this Court. The specific question as to the weight which should be given ultimate findings of fact or inferences of fact by the Tax Court based upon primary or subsidiary findings of fact contrary to the undisputed evidence has not been but should be decided by this Court.

Res adjudicata in tax matters, the validity of family partnerships for income tax purposes, and the question of what constitutes "substantial evidence"—the three principal issues involved in this case—are federal questions of the highest importance. The decisions of this Court relating to those questions do not cover many phases of the two subjects, and it is evident from the decisions of the lower Courts that they have found difficulty in applying the principles enunciated in the decisions of this Court which deal with those questions or with related matters.[1] We urge, therefore, that this Court review the decision of the lower Court in this case and settle the important questions presented by this record.

Wherefore, your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Fifth Circuit commanding that Court to certify and to send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket, No. 11,276, *M. M. Argo, Petitioner,* v. *Commissioner of Internal Revenue, Respondent,* and that the said judgment of the United States Circuit Court of Appeals for the Fifth Circuit may be reversed by this Honorable Court, and that your peti-

---

[1] See the article by Robert J. Bird on *Res Judicata* in the August, 1945, issue of the magazine, *Taxes*

tioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just; and your petitioner will ever pray.

Respectfully submitted,

H. Cecil Kilpatrick,
Douglas Arant,
Counsel for petitioner.

Mills & Kilpatrick,
Washington, D. C.;
Ellene Winn,
Virginia Lloyd Dunlap,
Bradley, Baldwin, All & White,
Birmingham, Alabama,
Of Counsel.

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1945

No. 436

M. M. ARGO,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

I

The Opinions of the Courts Below

The opinion in the Tax Court of the United States is reported in 3 T. C. 1120, was issued on September 30, 1944, and is shown on pages 83-90 of the record in this case. The opinion in the United States Circuit Court of Appeals for the Fifth Circuit is reported in 150 Fed. (2d) 67 (Adv.), was issued on June 20, 1945, and is shown on pages 162-165 of the record in this case.

II

Jurisdiction

(1) The jurisdiction of this Court is based on Section 240(a) of the Judicial Code, 28 U. S. C. A., Sec. 347, as amended by the Act of February 13, 1925.

(2) The date of the judgment to be reviewed is June 20, 1945 (R. p. 165).

III

Statement of the Case

In the interest of brevity, we are not stating again here the facts set forth in the Petition, under the heading, Summary Statement of the Matter Involved. Reference to that Statement is made.

We deem it inappropriate to include in this brief a detailed statement regarding the proceedings and the evidence before the Tax Court. We shall, however, briefly summarize the evidence relating to the question whether Birmingham Electric & Manufacturing Company, which was adjudicated by the former judgment to have existed as a partnership for income tax purposes throughout the year 1937, continued to be operated in the same manner during the years 1938, 1939, and 1940, the tax years here involved; and we shall briefly point out the evidence which is contrary to two of the statements of fact set forth in the opinion of the Tax Court.

Summary of Evidence as to Change in Company's Operations

The assets of the company were of the same character and of approximately the same value at the end of 1937 and at the end of each of the tax years here involved, i. e., 1938, 1939, and 1940 (R. pp. 118, 128, 137, 157). Cash

expenditures of the same character (the principal items each year being merchandise bought for sale, labor on materials for sale, other salaries and wages, auto and truck expense, and shop expense) were incurred each year in the following amounts: 1937, $120,882.89; 1938, $111,739.72; 1939, $119,439.22; 1940, $140,367.10 (R. pp. 111, 122, 132, 153). The "cost of goods sold" was as follows: 1937, $82,557.51; 1938, $80,066.98; 1939, $89,447.38; 1940, $102,-079.22 (Ibid.). The average number of employees each year was: 1937, 30; 1938, 26; 1939, 25; 1940, 27 (Respondent's Exhibits H-M, certified in original form).

Sarah Ellen Argo, one of the partners, and petitioner's youngest child, did no work for the partnership, either in 1937 or in the tax years here involved (R. p. 54). Esther B. Argo, petitioner's wife, did work of a clerical nature, without salary, "on many occasions," mostly on week ends and at night, during the years 1937, 1938, 1939, and 1940. "She worked more during the later years" (R. pp. 53, 60, 62). In 1937 and 1938, Malcolm M. Argo, Jr., a college student of engineering, and petitioner's oldest child, did part time work for the company without salary assisting with the management and working on electric equipment (R. p. 53, 56). Throughout 1939, and the first part of 1940, he attended college in another town. After he graduated as an electrical engineer in June 1940, he worked for the partnership "full time and overtime" until he entered the U. S. Army, Corps of Engineers, in October, 1940 (R. p. 57). In 1937 and 1939 and 1940, Ann Argo (later Ann Argo Dudley) worked on holidays and during vacations, without salary, doing filing and stenographic work. From October 1, 1940 (she having graduated from college in September 1940) until the end of the year, she worked full time, without salary, in the carbon brush department, doing general work in making brushes (R. pp. 53, 58, 59). During 1937 and the three tax years here involved, Mrs. Argo, Mal-

colm M. Argo, Jr., and Ann Argo had authority to draw and drew money from the bookkeeper of the partnership "whenever they needed it" (R. p. 53).

The petitioner, a graduate electrical engineer, acted as general manager throughout the years 1937, 1938, 1939, and 1940. He earned substantial amounts for work for persons other than the partnership, receiving $4,600.00 sales commission and $1,800.00 for professional services in 1939, and $2,000.00 for such services in 1940 (R. pp. 54, 78; petitioner's Exhibits 8 and 14, certified in original form). Under the partnership agreement, petitioner received $6,000.00 of the partnership annual profits and the remaining profits were divided equally between the other partners. The income distributed annually to each of the other four partners was as follows: 1937, $2,496.72; 1938, $1,988.48; 1939, $1,164.21;[2] 1940, $836.47 (R. pp. 121, 131, 140, 153).

As to the operations of the partnership during the years 1937 through 1940, Malcolm M. Argo, Jr., testified:

> "Throughout the years we had the same arrangement that my father made with us. There has been no change in the partnership from the first day of 1937 to the present." (R. p. 57)

Virginia Bayne, bookkeeper for the partnership, testified:

> "Since 1937 no change has occurred in the partnership accounts. It continued to operate on the same basis as in 1937." (R. p. 62)

---

[2] This figure is taken from the original return, showing $10,656.83 net income of the partnership, $6,000.00 distributed to petitioner, and $1,164.21 to each of the other four partners. As $4,600.00 of the total net income was subsequently conceded by petitioner to be his individual income from sales commissions (R. p. 78), the net income of the company was actually $6,056.83, leaving only $14.21 for each partner, after deducting the $6,000.00 due petitioner under the partnership agreement.

Evidence Contrary to Statements of Fact by the Tax Court

In its opinion, the Tax Court stated that it was not informed as to whether persons other than the partners were employed by the company. (R. p. 89) The record showed that the average number of persons employed, other than the partners, was as follows:

Year	*Employees*
1937	30
1938	26
1939	25
1940	27

(Respondent's Exhibits H-M, certified in original form.)

The Tax Court based its finding that petitioner had failed to show that his activities were not the main factors in producing the income of the company in part on its subsidiary finding that the annual earnings of the company were "50 per cent and more in excess of the capital investment in physical assets." This finding, in turn, was based on the figures shown by balance sheets of the company at the end of each year and fails to take into consideration money invested throughout the year.

The table set out below shows the total investment (including both physical assets at the beginning of the year and expenditures during the year), the larger items of expenditure, income, and percentages of return on the company's investment.

	1938	1939	1940
1. Physical Assets (land, buildings, machinery, inventory) at beginning of year	$24,874.40	$22,610.76	$18,817.45
2. Total expenditures	111,739.72	119,439.22	140,367.10
(a) Merchandise bought for sale	53,223.42	61,261.56	68,906.54
(b) Labor on materials for sale	26,353.62	26,576.89	34,118.15
(c) Other salaries and wages (excluding compensation to petitioner,)	11,512.00	10,377.75	10,863.00
(d) Auto and truck expense	3,159.71	2,593.24	2,644.88
(e) Shop expense	2,880.68	4,734.54	8,643.29
3. Total investment	136,614.12	142,049.98	159,184.55

	1938	1939	1940
4. Net income	13,953.91	6,056.83*	9,345.88
5. Percentage of return on above expenditures (Item 2)	12.49%	8.92%	6.66%
6. Percentage of return on Total Investment (including capital assets and expenditures during current year)	10%	4.2%	5.8%
7. 1/5 of Total Investment	27,322.82	28,410.00	31,836.91
8. Percentage of return to each partner other than petitioner	7.2%	.05%	2.6%

(R. pp. 111–115, 122–126, 132–135)

* $10,656.83, the figure shown as net income on the partnership return for 1939, is here corrected to $6,056.83, the remainder after deduction of $4,600.00, representing commissions conceded by petitioner to be taxable to him individually. (R. p. 78.)

IV

Specification of Errors

(1) The United States Circuit Court of Appeals for the Fifth Circuit erred in affirming the judgments of the Tax Court.

(2) The Circuit Court of Appeals erred in holding and deciding that the entire net income of the partnership, Birmingham Electric & Manufacturing Company, during the years 1938, 1939, and 1940 was taxable to the petitioner.

(3) The Circuit Court of Appeals erred in holding and deciding that the judgment of the United States District Court involving petitioner's tax liability for the year 1937 was not *res adjudicata* and did not operate as an estoppel by judgment as to the issues and questions here involved with respect to the year 1940.

(4) The Circuit Court of Appeals erred in failing to hold and decide that the Tax Court, in its consideration of the case involving the years 1938 and 1939, should have given weight to the former judgment of the District Court.

(5) The Circuit Court of Appeals erred in failing to hold contrary to law the decision of the Tax Court that

during the years 1938, 1939, and 1940, Birmingham Electric & Manufacturing Company was not a bona fide partnership for purposes of the federal income tax.

(6) The Circuit Court of Appeals erred in failing to decide and hold that the respondent has the burden of proving discontinuance of the partnership existence of which for income tax purposes has been once determined by the former judgment of the District Court.

(7) The Circuit Court of Appeals erred in failing to hold and decide that the partnership determined by the former judgment to have been in existence for income tax purposes during 1937 is presumed in the absence of proof to the contrary to continue to exist and to conduct its operations in the same manner.

(8) The Circuit Court of Appeals erred in failing to hold and decide that the following issues which were determined by the former judgment and which are material to a determination of the questions raised in the suit involving petitioner's income tax liability for the year 1940 were concluded by the former judgment:

> (a) The taxpayer on January 1, 1937, made valid bona fide gifts to members of his family of their several interests in the business.
>
> (b) The taxpayer on January 1, 1937, ceased to be the individual owner of the business and the several partners became the owners thereof.
>
> (c) A partnership valid for income tax purposes was formed January 1, 1937, and existed throughout that year.

(9) The Circuit Court of Appeals erred in holding and deciding that the adjudication by the District Court that a partnership valid for income tax purposes existed throughout the year 1937 does not estop the respondent from

asserting that no such partnership existed in 1940, when, according to the undisputed evidence in the instant case the business was conducted in the same fashion without substantial change of any kind from January 1, 1937, through the year 1940.

(10) The Circuit Court of Appeals erred in holding and deciding that the judgment of the District Court did not operate as *res adjudicata* or estoppel by judgment for the reason that the evidence presented to the jury in the trial of the former cause does not appear in the record of the case involving the year 1940.

(11) The Circuit Court of Appeals erred in holding and deciding that the decision of the Tax Court was supported by substantial evidence.

V

ARGUMENT

Summary of the Argument

Point A

The judgment of the District Court in the case of *Argo* v. *Willingham* is *res adjudicata* and operates as an estoppel to raise the issues there adjudicated which are material in the case involving the year 1940. In failing so to hold, the Circuit Court of Appeals rendered a decision which is not in accord with the applicable decisions of this Court, and which conflicts with the decision of the Circuit Court of Appeals for the Sixth Circuit in *Leininger* v. *Commissioner* (1936), 86 Fed. (2d) 791.

Tait v. *Western Maryland Railroad Co.* (1933), 289 U. S. 620, 53 S. Ct. 706, 77 L. ed. 1405;

Southern Pacific Railroad Co. v. *United States* (1897), 168 U. S. 1, 42 L. ed. 355, 18 S. Ct. 18;

Bates v. *Bodie* (1918), 245 U. S. 520, 62 L. ed. 444, 38 S. Ct. 182;.

The Last Chance Mining Co. v. *Tyler Mining Co.* (1894), 157 U. S. 683, 39 L. ed. 859, 15 S. Ct. 733;

New Orleans v. *Citizens Bank of Louisiana* (1897), 167 U. S. 371, 42 L. ed. 202, 17 S. Ct. 905;

Deposit Bank of Frankfort v. *Board of Councilmen* (1903), 191 U. S. 499, 48 L. ed. 276, 24 S. Ct. 154;

The Johnson Co. v. *Wharton* (1894), 152 U. S. 252, 38 L. ed. 429, 14 S. Ct. 608;

Leininger v. *Commissioner* (1934), 29 B. T. A. 874, affirmed (C. C. A., 6th 1936) 86 Fed. (2d) 791;

Donald v. *White Lumber Co.* (C. C. A., 5th 1934) 68 Fed. (2d) 441;

Commissioner v. *American Seating Co.* (1931), 50 Fed. (2d) 681;

Bennett v. *Commissioner of Internal Revenue* (C. C. A., 5th 1940) 113 Fed. (2d) 837, 130 A. L. R. 369;

Mary Haller (1932), 26 B. T. A. 395 (affirmed 68 Fed. (2d) 780);

Mayer v. *Kornegay* (1907), 152 Ala. 650, 44 So. 839;

Guin v. *Grasselli Chemical Co.* (1916), 197 Ala. 117, 72 So. 413;

Toy v. *Gong* (1918), 87 Ore. 454, 170 Pac. 936;

Kimmerle v. *Lowitz*, 203 Mich. 482;

Wood v. *Byington*, 2 Barb. Ch. (N. Y.) 387;

Hayes v. *Gudykunst*, 11 Pa. 221;

Bishop v. *Smith*, 9 Kan. App. 602, 58 Pac. 493;

Dutton v. *Woodman*, 9 Cush. (Mass.) 255;

2 Freeman on Judgments (5th Ed.) Sections 712; 900 et seq.; 904;

34 C. J., *Judgments*, Section 1313, page 905.

Point B

The judgment of the District Court in the case of *Argo* v. *Willingham* should have been given weight by the Tax Court in its consideration of the case involving the years 1938 and 1939. In failing so to hold, the Circuit Court of Appeals decided an important question of Federal law which has not been but which should be decided by this Court.

34 C. J., *Judgments*, Section 1508, p. 1067;
McDonald v. *Hannah* (Circ. Wash. 1892) 51 Fed. 73;
Coulson v. *Scott* (1910), 167 Ala. 606, 52 So. 436.

Point C

The decision of the Tax Court that Birmingham Electric & Manufacturing Company was not a bona fide partnership for income tax purposes in the years 1938, 1939, and 1940 was not supported by substantial evidence. In failing so to hold, the Circuit Court rendered a decision which is probably not in accord with the applicable decisions of this Court. The specific questions involved have not been but should be decided by this Court.

N. L. R. B. v. *Columbian E. & S. Co.* (1939), 306 U. S. 292, 83 L. Ed. 660, 59 S. Ct. 501;
N. L. R. B. v. *Thompson Products* (C. C. A., 6th, 1938) 97 Fed. (2d) 13;
Wilmington Trust Co. v. *Helvering* (1942), 316 U. S. 164, 86 L. Ed. 1352, 62 S. Ct. 984;
Helvering v. *Kehoe* (1940), 309 U. S. 277, 84 L. Ed. 751, 60 S. Ct. 549;
Helvering v. *Rankin* (1934), 295 U. S. 123, 79 L. Ed. 1343, 55 S. Ct. 732.

Point A

The judgment of the United States District Court for the Southern Division of the Northern District of Alabama is res adjudicata and gives rise to an estoppel by judgment to raise the issues there adjudicated and which are material in the case involving the year 1940.

The principle of *res adjudicata* or estoppel by judgment is clearly applicable in the case involving the year 1940 (Docket No. 112,248 in the Tax Court), in which the petition for review was filed in the Board of Tax Appeals (now the Tax Court) on August 24, 1942. The petition for review having been filed after June 15, 1942, the parties to the former action against the Collector in the District Court and those in the case here involving the year 1940 are deemed to be the same for the purpose of applying the principle of *res adjudicata* or estoppel by judgment. See Sec. 3772 (b) of the Internal Revenue Code (printed in the Appendix).

In its opinion, the Tax Court said with respect to the former case in the District Court and the case here involving the year 1940:

> "* * * the verdict of the jury and the judgment entered thereon involved a determination that there was a partnership for Federal income tax purposes in 1937. The question presented here in Docket No. 112,248 is the same except for different years, such question requiring a determination of whether there was a partnership for Federal income tax purposes between the same persons in the same business during the year 1940." (R. p. 86).

The principle of law applicable here has been many times enunciated in this Court and is succinctly stated in the case of *Southern Pacific R. Co.* v. *U. S.* (1897), 168 U. S. 1, 18 S. Ct. 18, 42 L. ed. 355, as follows:

> "The general principle announced in numerous cases is that a right, question, or fact distinctly put in issue,

> and directly determined by a court of competent jurisdiction, as a ground of recovery, cannot be disputed in a subsequent suit between the same parties or their privies; and, even if the second suit is for a different cause of action, the right, question, or fact once so determined must, as between the same parties or their privies, be taken as conclusively established, so long as the judgment in the first suit remains unmodified."

Applying that principle to tax matters, this Court has held that in an action for one year's taxes the parties are concluded as to the issues, rights and questions adjudicated by a former judgment respecting the tax of an earlier year. *Tait* v. *Western Md. R. Co.*, 289 U. S. 620, 53 S. Ct. 706, 77 L. ed., 1405. Directly in point with the instant cases is the decision of the Circuit Court of Appeals for the Sixth Circuit in the case of *Leininger* v. *Commissioner* (C. C. A. 6th, 1936), 86 Fed. (2d) 791. In that case the Commissioner taxed the taxpayer on one-half of the profits of the Eagle Laundry Company, a partnership (a one-half interest in which was owned by persons not related to the taxpayer) for the years 1920 to 1923. He owned a one-half interest in the partnership prior to the year 1920. He asserted that his wife had acquired one-half of his interest and had become a member of the partnership, and accordingly that she owned a twenty-five per cent interest and was taxable on twenty-five per cent of the profits, and that he owned a twenty-five per cent interest and was taxable on twenty-five per cent of the profits. The Board of Tax Appeals held that the taxpayer's wife was not a partner in the company. *Leininger* v. *Commissioner* (1930), 19 B. T. A. 621, affirmed 285 U. S. 136. Thereafter, for the years 1924-1929, inclusive, the Commissioner again taxed the taxpayer on one-half of the profits of the Company. The taxpayer appealed to the Board. It held that he was estopped by the former

judgment to assert that his wife was a partner in the Company. The Board said (29 B. T. A. 878):

> "As we have already pointed out, the years before us in the former proceedings were 1920 to 1923. The years now before us are 1924 to 1929. We have no doubt that if petitioner could prove that beginning with 1924 a new partnership agreement was entered into by which his wife became an actual partner in the Eagle Laundry Co. to the extent of a 25 per cent interest and petitioner became a partner to the extent of only a 25 per cent interest, he would be permitted to plead such an issue and offer proof in substantiation thereof and no doctrine of estoppel by judgment could prevent him from doing so. In such a case there would not only be a difference in the cause of action, in that the taxable years would be different, but there would be a new issue founded on different facts from those which existed in the prior years covered by the former proceedings. But petitioner does not contend that any new or different partnership agreement existed in the years 1924 to 1929 from that which existed in three of the years before us in the former proceedings, namely, 1921, 1922, and 1923."

* * * * * * *

> "It seems to us that the situation we have before us is not unlike that in *Tait v. Western Maryland Ry. Co., supra,* in which the Supreme Court affirmed the Circuit Court of Appeals in *Tait v. Western Maryland Ry. Co.,* 62 Fed. (2d) 933. In that case the Circuit Court, in affirming the District Court, said:
>
> " 'We are now asked to re-examine the evidence and reach a different conclusion, and the reasons given are that the evidence in the present case shows more clearly the gap between the present corporation and the one which originally issued the greater amount of the bonds; and also that this court did not fully appreciate the force of the facts in the former case which marked the difference between the present company and the

one which immediately preceded it. We are not impressed by this argument for if a question is actually and directly in issue and is judicially passed upon and determined in a suit, a party bound by the judgment cannot escape its effects by producing a new argument or new evidence in a subsequent action in support of the proposition decided against him. * * * If the appellee in the pending case is now permitted to produce additional evidence (which it may be said in passing was available at the first trial), to prove the point which was then relied on, the settled rule would be disregarded and the purpose of the doctrine of *res adjudicata* to put an end to litigation and to protect a successful litigant from a second trial of a controversy would be defeated.'

"Under the authorities above cited, we hold that the judgment of the Supreme Court in the former proceedings is an estoppel against the contentions made by petitioner in these proceedings."

The Circuit Court of Appeals for the Sixth Circuit affirmed the decision of the Board. 86 Fed. (2d) 791. The Court said:

"Assuming that this evidence was sufficient to reduce petitioner's interest in the partnership to 25 per cent, his difficulty is, that although this may have been his actual status at the beginning of the tax year 1920, the Supreme Court decided this very issue, that is, the extent of his interest, against him in the former proceeding and its decision is undoubtedly conclusive against his present contention, although different tax years are involved. See *Tait* v. *Western Maryland Ry. Co.*, 289 U. S. 620, 623, 53 S. Ct. 706, 707, 77 L. Ed. 1405; *United Shoe Mach. Corp.* v. *U. S.*, 258 U. S. 451, 458, 42 S. Ct. 363, 365, 66 L. Ed. 708; *Bates* v. *Bodie*, 245 U. S. 520, 526, 38 S. Ct. 182, 62 L. Ed. 444, L. R. A. 1918 C, 355; *Radford* v. *Myers*, 231 U. S. 725, 730, 34 S. Ct. 249, 58 L. Ed. 454; *Cromwell* v. *County of Sac*, 94 U. S. 351, 370, 24 L. Ed. 195; *Sutton* v. *Wentworth*, 247 F. 493, 501 (C. C. A. 1); *Santos* v. *Moreda*, 71 F.

(2d) 608, 609 (C. C. A. 1). The extent of petitioner's interest having been determined in the first suit, the question may not be relitigated in the second. If petitioner should now be permitted to introduce evidence available on the first hearing, or new evidence, or advance a different theory to sustain the contention decided against him in the first action, the purpose of *res adjudicata* would be frustrated. *Southern Pac. R. Co.* v. *U. S.*, 168 U. S. 1, 18 S. Ct. 18, 42 L. Ed. 355; *Tait* v. *Western Maryland Ry. Co.*, 62 F. (2d) 933, 935 (C. C. A. 4)."

The reasoning of the Circuit Court of Appeals is likewise applicable here: "The extent of petitioner's interest having been determined in the first suit, the question may not be relitigated in the second." 86 Fed. (2d), at p. 792.

The Tax Court based its decision that the former judgment did not operate as an estoppel in the case involving the year 1940 upon the fact that the evidence submitted to the jury upon the former trial did not appear in the record of the instant case. The pleadings, order on pretrial hearing, and the order of judgment in the former case in the District Court, however, were in evidence. (R. p. 141-161) The undisputed evidence in the instant case clearly shows, moreover, that the material facts respecting the operation of the partnership and its business during 1940 were the same as those existing in 1937.

In the many decisions in which it is held that a judgment as to some question or fact therein adjudicated operates as an estoppel in a subsequent cause of action in which the same question or fact is material, it is uniformly held that only the fact of the prior judgment need be proved, and that it is immaterial upon what evidence it was based.

In *Southern Pacific R. Co.* v. *U. S.*, *supra*, the controlling matter in issue in both the prior case and the pending controversy was whether certain maps filed by the At-

lantic and Pacific Ry. Co. in 1872 (prior to either decision) were valid maps of definite location. It was held that a fact once established and made the basis of a decree could not thereafter be disputed in a second suit, even upon a different cause of action, but that "the thing adjudged" must be "received in evidence 'as irrefragable truth' ". The Court concluded, after a detailed consideration of the pleadings and judgment in the former case that the issue in the former case and that in the pending controversy were the same. It was obviously not considered essential to examine or to discuss the evidence in the earlier case. After quoting with approval the statement from the opinion in *Last Chance Mining Company* v. *Tyler, infra,* to the effect that the relevant inquiry, in such case, is whether a fact has been judicially determined and not upon what evidence it was determined, the Court held:

> "* * * it would seem that *the controlling inquiry is whether, under the pleadings in the former cases, the sufficiency of the Atlantic & Pacific maps of 1872 as maps of definite location was a matter in issue and determined,* as between the United States and the Southern Pacific Railroad Company. That that matter was in issue and was actually decided in the former cases, is too clear to admit of doubt. That it was material is equally clear;" (Italics supplied)

In *Bates* v. *Bodie* (1918) 245 U. S. 520, 62 L. Ed. 444, 38 S. Ct. 182, this Court, in discussing when a judgment operated as an estoppel to raise questions therein determined said:

> "But how find the matters in issue or the points controverted upon the determination of which the judgment was rendered? The obvious answer would seem to be that for the issues we must go to the pleadings; for response to them and their determination, to the judgment; and each may furnish a definition of the other."

In *Last Chance Mining Company* v. *Tyler Mining Company* (1894) 157 U. S. 683, 39 L. Ed. 859, 15 S. Ct. 733, the issues decided by a judgment relied on as giving rise to an estoppel were determined by reference to the findings of fact, the pleadings, and the judgment itself. It was objected that the applicable state statutes did not provide for findings of fact in such a case, and, further, that there was only a judgment by default. The Court held that the complaint and the judgment nevertheless established what issues were adjudicated, and that it was immaterial upon what evidence the judgment was reached. The opinion reads in part:

> "* * * if we ignore the findings altogether and look simply at the judgment and the complaint, this appear: The single ground stated in the complaint upon which superiority of right is claimed is priority of location. A judgment for the plaintiffs upon such a complaint is necessarily an adjudication in favor of that priority of location. There is no other fact upon which it can rest. * * *
>
> "The essence of estoppel by judgment is that there has been a judicial determination of a fact, and the question always is, has there been such determination, and not upon what evidence or by what means was it reached. * * *"

In *Tait* v. *Western Maryland Ry. Co.* (C. C. A. 4th, 1933) 62 F. (2d) 933 (affirmed in this Court in 289 U. S. 620, 53 S. Ct. 660, 77 L. Ed. 1405) it was held that a prior decision permitting deduction for income tax purposes of the amortized portion of the discount on certain bonds for the years 1918 and 1919 operated as an estoppel in a subsequent action involving the years 1920 and 1925. As to the contention that different and material facts with respect to the history of the taxpayer's predecessor corporations were presented in the later controversy and that the doc-

trine of *res adjudicata* was therefore inapplicable, the Court said:

> "• • • We are not impressed by this argument, for if a question is actually and directly in issue, and is judicially passed upon and determined in a suit, a party bound by the judgment cannot escape its effects by producing a new argument or new evidence in a subsequent action in support of the proposition decided against him. • • •"

See also *New Orleans* v. *Citizens Bank of Louisiana* (1897) 167 U. S. 371, 42 L. Ed. 202, 17 S. Ct. 905; *Deposit Bank of Frankfort* v. *Board of Councilmen* (1903) 191 U. S. 499, 48 L. Ed. 276, 24 S. Ct. 154; *The Johnson Co.* v. *Wharton* (1894) 152 U. S. 252, 38 L. Ed. 429, 14 S. Ct. 608.

In *Donald* v. *White Lumber Co.* (C. C. A., 5th 1934), 68 F. (2d) 441, the court held that a former judgment as to the value of certain timber as of March 1, 1913 was conclusive evidence of such value in a subsequent action in which such value was a material issue. The District Court "had before it and considered all the pleadings, its own findings of fact, conclusions of law and the judgment in the prior suit tried before it." The Circuit Court of Appeals held that the District Court correctly decided that the prior judgment worked an estoppel as to the value of the timber in 1913, it being said:

> "A prior judgment is conclusive evidence as to all matters in issue and thereby determined in a subsequent suit upon a different cause of action between the same parties or their privies."

It will be noted that the evidence upon which the prior judgment was based was not introduced in evidence and that the Court apparently deemed this omission immaterial.

In case of *Mary Haller* (1932) 26 B. T. A. 395 (affirmed 68 F. (2d) 780) concerns the existence of a partnership for

income tax purposes. In a proceeding respecting income taxes for the years 1924 and 1925 the Commissioner pleaded *res adjudicata,* contending that the questions of law and fact raised by the petitioner had been decided adversely to her by an earlier decision of the Board of Tax Appeals. At the hearing in the latter case, "the pleadings in those proceedings which involved the years 1917 to 1923 * * * the Board's decision and the orders of redetermination were submitted and received in evidence." It is clear that the evidence before the Board in the earlier case was not introduced in evidence. Mary Haller contended that under the will of her husband, who died in 1895, the income from a grocery business was distributable 1/7 to her and 1/7 to each of her children during the years 1924 and 1925 and further, that an agreement between herself and her children had created a partnership during the years 1924 and 1925. The Board held that substantially the same questions had been raised and decided in the former proceeding and that the former decision precluded Mary Haller "from asserting that a partnership in the profits of the grocery business *existed at any time during the years in controversy in the former proceedings, i. e., prior to January 1, 1924*"; and that "in accordance with the same principles our former decision is conclusive as to the construction of the will of Jacob Haller and the codicil thereto to the effect that under the will the children of Jacob Haller had no legal interest in the net profits of the grocery business."

In the case of *Bennett* v. *Commissioner of Internal Revenue* (C. C. A. 5th 1940), 113 Fed. (2d) 837, 130 A. L. R. 369, it was held that a judgment that a taxpayer was liable on an endorsement of certain notes and that he could take a bad debt deduction when he paid one of them in 1934 was *res adjudicata* as to similar notes which he took up in 1935 under the same circumstances. The taxpayer

pleaded *res adjudicata* by reason of the decision of a district court respecting the note taken up in 1934 and attached to his pleading "certified copies of the pleadings, the findings of fact, the conclusions of law, the opinion of the court and the judgment in that case". The Circuit Court of Appeals held that the Commissioner was estopped by the judgment of the District Court from contending that the point in issue was otherwise than as there adjudged. No reference was made to the necessity for introducing the evidence upon which the said judgment of the District Court was based.

See also the case of *Commissioner of Internal Revenue* v. *American Seating Company* (C. C. A. 7th 1931), 50 F. (2d) 681, in which it was held, in spite of the express objection that the evidence in the prior case was not submitted in evidence, that findings of fact by the Board of Tax Appeals were *prima facie* evidence, in a later case, of the truth of the findings.

It is clear from the authorities cited that if the facts and issues determined by the prior judgment are material here, that judgment, properly introduced in this case, constitutes conclusive evidence of such facts and issues, and operates as an estoppel to raise them again. It is clear, further, that only the judgment, and not the evidence in the prior case, need be proved.

To ascertain the extent to which the former judgment is an estoppel, therefore, the inquiry is, first, what issues, questions and facts were decided by that judgment, and, second, which of those issues, questions and facts are material here. The following questions were necessarily decided by the former judgment:

> (1) The taxpayer on January 1, 1937, made valid bona fide gifts to members of his family of their several interests in the business.

(2) The taxpayer on January 1, 1937, ceased to be the individual owner of the business and the several partners became the owners thereof.

(3) A partnership valid for income tax purposes was formed January 1, 1937, and existed throughout that year.

These questions are clearly material and, indeed, controlling here. It is obvious from the findings of fact and the opinion of the Tax Court that it based its decision upon the theory that no partnership, valid for income tax purposes, *had ever been formed;* that the "economic status" of the petitioner *had never changed,* and that he remained the individual owner of the business. The brief resume of facts in the opinion of the Circuit Court of Appeals reveals that its decision, also, is predicated upon the view that no partnership valid for income tax purposes *was ever formed.* The Government has never contended that the operations of the partnership have changed in any way since 1937.

These issues are, further, material and controlling in the instant case because of the fact that it is presumed, in the absence of evidence to the contrary, that the facts as they existed at the time of the former judgment continued to exist: In 34 C. J., *Judgments,* Sec. 1313, page 905, it is said:

> "The estoppel of a judgment extends only to the facts in issue as they existed at the time the judgment was rendered, and does not prevent a reexamination of the same questions between the same parties where in the interval the facts have changed or new facts have occurred which may alter the legal rights or relations of the litigants. But in the absence of evidence to the contrary the facts as they existed at the time of the former judgment will be presumed to continue."

It has been frequently held that where the fact of a partnership is litigated and determined it becomes *res adjudicata* in subsequent actions where the same issue comes into ques-

tion. *Toy* v. *Gong*, 87 Ore. 454, 170 Pac. 936; *Kimmerle* v. *Lowitz*, 203 Mich. 482; *Wood* v. *Byington*, 2 Bard. Ch. (N. Y.) 387; *Hayes* v. *Gudykunst*, 11 Pa. 221; *Bishop* v. *Smith*, 9 Kan. App. 602, 58 Pac. 493; *Dutton* v. *Woodman*, 9 Cush. (Mass.) 255; 2 Freeman on *Judgments* (5th Ed.), Section 904. The status adjudicated in the first case is presumed to continue until facts showing a change are proved. *Mayer* v. *Kornegay* (1907), 152 Ala. 650, 44 So. 839; *Guin* v. *Grasselli Chemical Co.* (1916), 197 Ala. 117, 72 So. 413.

The presumption that the facts remain as they were at the time of the former judgment renders that judgment of controlling importance here, in view of the Tax Court's finding that the evidence before it afforded "no basis for a positive finding" that a valid partnership for income tax purposes did not exist in the tax years in question. (R. 90) The fact of the existence of a bona fide partnership for income tax purposes throughout the year 1937, established by the former judgment, shifts the burden of proof to the Government. This burden, it is clear from the Tax Court's finding, the Government failed to meet.

Point B

Weight should have been given the decision of the District Court in the case of Argo v. Willingham by the Tax Court in its consideration of the case involving the years 1938 and 1939.

The principle of *res adjudicata* or estoppel by judgment would be applicable to the case involving the years 1938 and 1939, but for the technical rule that as to proceedings filed with the Board of Tax Appeals before June 15, 1942, the Collector is not in privity with the Commissioner. See *United States* v. *Nunnally Investment Company* (1942), 316 U. S. 258, 86 L. Ed. 1455, 62 S. Ct. 1064; Sec. 3772 (b), Internal Revenue Code, printed in the Appendix. The

petition to review involving those two years was filed before June 15, 1942. It has been demonstrated, we believe, that the judgment of the District Court is conclusive against the respondent in the case involving the year 1940. In reality and in substance the question whether the partnership was a bona fide partnership for Federal income tax purposes was tried and settled by the District Court. The Government first took an appeal to this Court, but later moved to dismiss the appeal and acquiesced in the judgment. The record shows that the situation in all material respects remained the same. It seems clear that even if, for the reason above indicated, the former judgment is not conclusive in the case involving the years 1938 and 1939, it is entitled to great weight as evidence in that case. To disregard it entirely is to ignore the substance of that matter. Furthermore, as we have pointed out, the status of the petitioner with respect to the partnership for income tax purposes having been adjudicated, it is presumed to continue in the absence of evidence to the contrary. The former judgment adjudicated that the partnership was formed on January 1, 1937, was thereafter operated in good faith, and was valid for income tax purposes. Irrespective of any technical question of privity as between the Commissioner and the Collector, great weight should have been given to the former judgment by the Tax Court in its consideration of the case involving the years 1938 and 1939.

The general rule with respect to the weight to be given former judgments in subsequent cases involving different parties is stated as follows in 34 C. J., *Judgments*, Sec. 1508, page 1067:

> "Aside from the question of its conclusiveness as a bar or estoppel, a judgment is admissible and competent evidence * * * as persuasive although not conclusive, evidence of the facts which it adjudges or determines, even as against strangers."

See also *McDonald* v. *Hannah* (Circ. Wash. 1892), 51 Fed. 73; *Coulson* v. *Scott* (1910), 167 Ala. 606, 52 So. 436.

We submit that this rule applies here with peculiar force in view of the fact that the Government is actually the party in interest in both cases and that the technical rule of want of privity between the Collector and the Commissioner is based merely upon the artificial consideration that the Collector is sued in his personal capacity.

In failing to hold that the Tax Court erred in giving no weight to the former judgment in its consideration of the cases involving the years 1938 and 1939, the Circuit Court of Appeals decided an important Federal question which has not been but which should be decided by this Court.

Point C

The decision of the Tax Court that Birmingham Electric & Manufacturing Company was not a bona fide partnership for income tax purposes in the years 1938, 1939 and 1940 was not supported by substantial evidence.

Under the rule often announced, the decisions of the Tax Court must be supported by "substantial evidence." *Helvering* v. *Kehoe* (1940), 309 U. S. 277, 84 L. Ed. 751, 60 S. Ct. 549; *Wilmington Trust Co.* v. *Helvering* (1942), 86 L. Ed. 1352, 316 U. S. 164, 62 S. Ct. 984; *Helvering* v. *Rankin* (1934), 295 U. S. 123, 79 L. Ed. 1343, 1349, 55 S. Ct. 732.

In *N. L. R. B.* v. *Columbian E. & S. Co.* (1939), 306 U. S. 292, 83 L. Ed. 660, 59 S. Ct. 501, "substantial evidence" is defined as follows:

> "Substantial evidence is more than a scintilla, and must do more than create a suspicion of the existence of the fact to be established. 'It means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion,' Consolidated Edison Co. v. National Labor Relations Bd., 305 U. S. 197, ante, 126, 59 S. Ct. 206, supra, and *it must be enough to*

justify, if the trial were to a jury, a refusal to direct a verdict when the conclusion sought to be drawn from it is one of fact for the jury."

A similar definition in *N. L. R. B.* v. *Thompson Products* (C. C. A. 6th, 1938), 97 Fed. (2d) 13, is as follows:

> "'Substantial evidence' means more than a mere scintilla. It is of substantial and relevant consequence and excludes vague, uncertain, or irrelevant matter. It implies a quality of proof which induces conviction and makes an impression on reason. It means that the one weighing the evidence *takes into consideration all the facts presented to him and all reasonable inferences, deductions and conclusions to be drawn therefrom and, considering them in their entirety and relation to each other, arrives at a fixed conviction.*
>
> "The rule of substantial evidence is one of fundamental importance and is the dividing line between law and arbitrary power. Testimony is the raw material out of which we construct truth and, *unless all of it is weighed in its totality,* errors will result and great injustices be wrought."

The Tax Court failed to consider all the relevant evidence before it in that it disregarded the former judgment of the District Court which (as we have shown under Points A and B) constituted, with respect to the year 1940, conclusive evidence and, with respect to the years 1938 and 1939, persuasive evidence of facts material to a determination of the instant case.

The Tax Court stated that the evidence before it afforded "no basis for a positive finding that the activities and services of the petitioner were the main factors in the production of the income" of the partnership. If the Tax Court had considered the said judgment as evidence of the facts therein found, it is clear that in the absence of evidence affording such a "positive finding" the Tax Court would have been compelled to find that a bona fide partnership for

income tax purposes existed during the taxable years. The ultimate finding of the Tax Court is, therefore, based upon an exclusion of and a failure to consider material evidence shifting the burden of proof to the Commissioner and its said ultimate finding is, therefore, unsupported by substantial evidence.

Further, the Tax Court's finding that the petitioner failed to show "that his activities and services were not the main factors in the production of the income" of the company is based upon two subsidiary findings which are directly controverted by the evidence. The Tax Court stated, in its opinion:

> "We are not informed as to whether other persons were employed." (R. 89)

The average number of employees in the business during the tax years was shown by the evidence to be as follows:

Year	Employees
1938	26
1939	25
1940	27

(See respondent's Exhibits H-M, certified in original form.)

The Tax Court based its inference that petitioner had failed to show that his services were not the main factors in the production of the partnership income in large measure on its subsidiary finding that the partnership's annual earnings were "50 per cent and more in excess of the capital investment in physical assets." An analysis of the evidence shows, as is demonstrated in the statement of facts herein, that the percentage of return upon the company's investment, including current expenditures for merchandise, labor, etc., was, during the tax years, actually less than ten per cent. The inference based on this sub-

sidiary finding clearly ignores material and controlling evidence as to the factors which produced the partnership income.

It is clear that inferences of fact and ultimate findings which are based on subsidiary findings directly controverted by the record are not supported by substantial evidence.

In *Wilmington Trust Co.* v. *Helvering, supra,* inferences of fact found by the Board of Tax Appeals were not disturbed because it appeared that such inferences were based upon subsidiary findings of fact which were supported by substantial evidence. It follows that inferences of fact by the Tax Court are not conclusive when based upon subsidiary findings which are directly controverted by the evidence.

In failing to hold that the decision of the Tax Court in this case was unsupported by substantial evidence, the Circuit Court of Appeals decided an important question of Federal law in a manner which is probably not in accord with the applicable decisions of this Court and which involves important questions of Federal law which have not been but which should be decided by this Court.

Conclusion

The petition for a writ of certiorari should be granted.

Respectfully submitted,

H. Cecil Kilpatrick,
Douglas Arant,
Counsel for Petitioner.

Mills & Kilpatrick,
Washington, D. C.;
Ellene Winn,
Virginia Lloyd Dunlap,
Bradley, Baldwin, All & White,
Birmingham, Alabama;
Of Counsel.

APPENDIX

Internal Revenue Code:

Sec. 3772 (As amended by Section 503 of the Revenue Act of 1942, c. 619, 56 Stat. 798). SUITS FOR REFUND.

* * * * * * *

(d) *Suits Against Collector a Bar.*—A suit against a collector (or former collector) or his personal representative for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected shall be treated as if the United States had been a party to such suit in applying the doctrine of res judicata in all suits instituted after June 15, 1942, in respect of any internal revenue tax, and in all proceedings in the Board and on review of decisions of the Board where the petition to the Board was filed after such date.

(26 U. S. C., 1940 ed., Sec. 3772.)

Sec. 181. PARTNERSHIP NOT TAXABLE

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Questions presented	2
Statutes involved	2
Statement	4
Argument	16
Conclusion	21

CITATIONS

Cases:

Bankers Coal Co. v. *Burnet*, 287 U. S. 308	16, 17
Burnet v. *Leininger*, 285 U. S. 136	19
Campana Corp. v. *Harrison*, 135 F. (2d) 334	18
Commissioner v. *Court Holding Co.*, 324 U. S. 331	20
Commissioner v. *Netcher*, 143 F. (2d) 484, certiorari denied, 323 U. S. 759	18
Commissioner v. *Tower*, No. 317, October Term, 1945	20
Commissioner v. *Western Union Tel. Co.*, 141 F. (2d) 774	18
Dobson v. *Commissioner*, 320 U. S. 489, rehearing denied, 321 U. S. 231	19
Doll v. *Commissioner*, No. 138, October Term, 1945	21
Engineers' Club of Philadelphia v. *United States*, 42 F. Supp. 182, certiorari denied, 316 U. S. 700	18
Griffiths v. *Commissioner*, 308 U. S. 355	20
Harrison v. *Schaffner*, 312 U. S. 579	20
Helvering v. *Eubank*, 311 U. S. 122	20
Helvering v. *Horst*, 311 U. S. 112	20
Henricksen v. *Seward*, 135 F. (2d) 986	18
Leicht v. *Commissioner*, 137 F. (2d) 433	19
Leininger v. *Commissioner*, 86 F. (2d) 791	18
Lucas v. *Earl*, 281 U. S. 111	20
Lusthaus v. *Commissioner*, No. 263, October Term, 1945	20
Monteith Bros. Co. v. *United States*, 142 F. (2d) 139	18
Montgomery v. *Thomas*, 146 F. (2d) 76	17
Pelham Hall Co. v. *Hassett*, 147 F. (2d) 63	18
Russell v. *Place*, 94 U. S. 606	19
Sage v. *United States*, 250 U. S. 33	17
Stoddard v. *Commissioner*, 141 F. (2d) 76	18
Tait v. *Western Md. Ry. Co.*, 289 U. S. 620	17

669749—45——1

Cases—Continued Page
United States v. *Nunnally Investment Co.*, 316 U. S. 258 ..... 16, 17
Webre Steib Co. v. *Commissioner*, 324 U. S. 164 17
Statutes:
Internal Revenue Code:
Sec. 22 (26 U. S. C., Sec. 22) 3
Sec. 181 (26 U. S. C., Sec. 181) 3
Sec. 3772 (26 U. S. C., Sec. 3772) 3, 16
Revenue Act of 1938, c. 289, 52 Stat. 447:
Sec. 22 2
Sec. 181 3

In the Supreme Court of the United States

OCTOBER TERM, 1945

No. 436

M. M. ARGO, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of The Tax Court of the United States (R. 68–91) is reported in 3 T. C. 1120. The opinion of the Circuit Court of Appeals (R. 162–165) is reported in 150 F. (2d) 67.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on June 20, 1945. (R. 165.) The petition for a writ of certiorari was filed on September 18, 1945. The jurisdiction of this Court

is invoked under Section 240 (a) of the Judicial Code, as amended.

QUESTIONS PRESENTED

1. Whether the Commissioner is precluded from attacking the recognition of a family partnership for tax purposes for the years 1938, 1939 and 1940 by reason of the judgment of the District Court in favor of taxpayer and against the Collector for the recovery of income taxes for the year 1937.

2. Whether there is any warrant in the record for the Tax Court's conclusion that a family partnership arrangement involving the taxpayer, his wife, and three children should not be recognized for tax purposes and hence that the income from the business for the years 1938, 1939 and 1940 remained taxable to the taxpayer under Section 22 (a) of the Revenue Act of 1938 and of the Internal Revenue Code.

STATUTES INVOLVED

Revenue Act of 1938, c. 289, 52 Stat. 447:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such

property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *

* * * * *

SEC. 181. PARTNERSHIP NOT TAXABLE.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

The corresponding provisions of the Internal Revenue Code are identical.

Internal Revenue Code:

SEC. 3772. [as amended by the Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 503]. SUITS FOR REFUNDS.

* * * * *

(d) *Suits Against Collector a Bar.*—A suit against a collector (or former collector) or his personal representative for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected shall be treated as if the United States had been a party to such suit in applying the doctrine of res judicata in all suits instituted after June 15, 1942, in respect of any internal revenue tax, and in all proceedings in the Board and on review of decisions of the Board where the peti-

tion to the Board was filed after such date. (26 U. S. C., Sec. 3772.)

STATEMENT

The facts as found by the Tax Court may be summarized as follows (R. 70–83):

During 1936 taxpayer owned all the capital stock of the Birmingham Electric & Manufacturing Company, a corporation organized under the laws of Alabama, and engaged in the business of repairing and rebuilding electrical machinery and equipment. The business, both while operated as a corporation and as an unincorporated concern, was of a type requiring technical knowledge. Taxpayer is a graduate electrical engineer and he has been engaged in that profession since 1912. He was president of the corporation and received a salary for the year 1936 of $12,000. (R. 70.)

During 1936 taxpayer discussed with an attorney, an auditor, and a certified public accountant the question of dissolving the corporation and forming a partnership consisting of himself, his wife, and his three minor children. The possibility of a saving in income taxes was also discussed. Taxpayer's attorney advised him to form the partnership and stated it could be accomplished legally without the execution of a written agreement. The proposed partnership was also discussed by taxpayer during the latter part of 1936 with his wife, Esther B. Argo, and his chil-

dren, Malcolm M. Argo, Jr., then of the age of 18, Ann A., then of the age of 16, and Sarah Ellen, then of the age of 7. Malcolm M. Argo, Jr., became of age on July 9, 1939, and Ann A. Argo in January, 1941. As a final result of these discussions taxpayer told his wife and children that he was going to dissolve the corporation and was going to make an outright gift to each of them of a one-fifth interest in the partnership and that they would be partners with him and be responsible for any debts of the partnership. It was understood that taxpayer was to receive $6,000 a year from the profits and would manage the business, with the right to operate it as he saw fit. The profits after deducting the taxpayer's $6,000 per annum were to be distributed equally among the other four members of the family. (R. 70–71.)

At that time taxpayer's wife owned no property except the family home, which was encumbered by a mortgage on which taxpayer was liable. Her occupation was that of a housewife, and she was without any income other than a small amount derived from writing. The occupation of the children was that of attending school and they had no property or income. (R. 71.)

During the time that the business was operated as a corporation taxpayer's wife frequently helped with the office work, his son worked for the business during his school vacations, and his oldest

daughter also worked for the business during her school vacations. (R. 71.)

On December 31, 1936, the Birmingham Electric & Manufacturing Company, the corporation, was dissolved, and taxpayer, as its sole stockholder, received all its assets and assumed its liabilities. These assets were immediately credited to an unincorporated business which thereafter conducted the same character of business as had the corporation and under the same name as that of the corporation. This unincorporated business will be sometimes referred to hereinafter as the company. (R. 71–72.)

Taxpayer instructed his bookkeeper to make entries on the company's books dividing interests in the company equally among the five members of the family, and he told her that he was making a gift to his wife and children of those interests. She was also told that taxpayer was to receive $6,000 annually from the profits and the remaining profits were to be distributed equally among the other four members of the family. In January, 1937, capital accounts were opened on the books crediting each member of the family with a total of $4,317.58. (R. 72.)

Taxpayer did not execute any deed, bill of sale, or other written form of conveyance transferring any interest in the business to his wife or children. After January 1937 the every-day operations of the company continued in the same

manner and under the same name as during incorporation, except for capital accounts, and for accounts of withdrawals by each of the members of the family in the case of the company. Taxpayer continued to handle and control the affairs of the company as he had in the case of the corporation. (R. 72.)

During the taxable years taxpayer's wife assisted in the business of the company when it was convenient for her to do so at night, as she was attending to her household affairs during the day, or on Saturday afternoon. She did clerical work, filing, and typing letters. She received no salary. (R. 74.)

Taxpayer's son Malcolm, Jr., attended college throughout 1937, except for the summer vacation period, during most of which period he assisted in the business of the company during afternoons in the shop and on night emergency calls when pumps or motors in coal mines were damaged by electrical storms. He also assisted his father during that year in managing the business. During the first half of 1938 he was away at college and during the remainder of the year, except while on a vacation in Cuba, he attended a local college during the morning and worked in the company warehouse in the afternoon, repairing and reconditioning motors. He attended college throughout 1939 and until graduating as an electrical engineer in June, 1940, when he began

working for the company on a full time basis, continuing to do so until he enlisted in the Army in October, 1940. He received no salary. (R. 74.)

Taxpayer's daughter Ann was away at college during 1937, except for a summer vacation, during half of which she attended a local college in the mornings. In the afternoons when not in school she helped in the business with filing and stenographic work. She did no work in 1938, being away at school during both the regular and summer terms. She did no work in 1939. In 1940 she did no work until October, after graduation. The balance of that year she worked regularly in the office or in the plant, operating machines and helping make carbon brushes. She received no salary. Taxpayer's daughter, Sarah Ellen, did no work for the company at any time. (R. 74.)

For the years 1937, 1938, 1939 and 1940 the company books in the various capital accounts of taxpayer, his wife and his three children, the partnership returns of income filed by taxpayer, and the individual income tax returns filed by the members of the family show net distributable profits as follows (R. 76, 78):[1]

[1] In the printed record, several tables have been shifted. For example, the table shown here appears in the printed record under the designation of drawing accounts (R. 78); whereas, in the original record it appears under the designation of distributable profits. Again, the first table designated as checks drawn to the order of the taxpayer in reality represents the drawing accounts. (R. 78.)

	1937	1938	1939	1940
M. M. Argo	$6,000.00	$6,000.00	$6,000.00	$6,000.00
Esther B. Argo	2,496.72	1,988.47	1,164.21	826.47
Malcolm M. Argo, Jr	2,496.72	1,988.48	1,164.21	826.47
Ann A. Argo	2,496.72	1,988.48	1,164.21	826.47
Sarah Ellen Argo	2,496.72	1,988.48	1,164.20	826.47
	15,986.88	13,953.91	10,656.83	9,305.88

The above listed profits of $10,656.83 in 1939 include $4,600 in personal commissions now conceded by taxpayer to be his individual income, taxable to him as such. (R. 78.)

There were no drawing accounts on the books for taxpayer's wife and children during 1937. All withdrawals by or for them during that year, totaling $7,650, were charged to taxpayer on the books. Neither taxpayer's wife nor his children had authority at any time to draw checks on the company's bank account. (R. 78.)

Drawing accounts on the books of the company reflect withdrawals for the years 1938, 1939 and 1940 as follows (R. 78):

	1938	1939	1940
M. M. Argo	$6,000.22	$4,934.39	$2,481.55
Esther B. Argo	1,240.10	1,364.66	2,983.67
Malcolm M. Argo, Jr	1,117.33	1,432.62	1,324.20
Ann A. Argo	688.97	1,551.12	1,219.17
Sarah Ellen Argo	65.10	1,155.62	1,243.67
	9,111.72	10,438.41	9,252.26

The withdrawals totaling $10,438.41 for 1939 include erroneous charges for withdrawals not in fact made, in the amount of $4,600, charged to

the extent of $600 against taxpayer's account and $1,000 against each of the remaining accounts. (R. 78.) The foregoing drawing accounts of taxpayer's wife and children, and the amount of withdrawals listed as above therein, also include a number of items based on checks drawn to the order of taxpayer and deposited in his individual bank account as follows (R. 79):

	1938		1939		1940	
	Number of checks	Amount	Number of checks	Amount	Number of checks	Amount
Esther B. Argo	2	$300.00				
Malcolm M. Argo, Jr.	6	750.00	2	$125.00		
Ann A. Argo					2	$247.40
Sarah Ellen Argo					1	625.00
	8	1,050.00	2	125.00	3	872.40

Taxpayer's wife had an allowance for running the house and would obtain what money she needed from the bookkeeper for household and personal expenses. Her withdrawals represented these amounts, except those represented by the checks deposited as above shown to taxpayer's individual bank account. (R. 79.)

There were no "dollars and cents" restrictions on Malcolm Jr.'s withdrawals. When he needed money he would ask the bookkeeper for it and she would let him have it. Ann made her withdrawals by asking her father or the office for them. She did not have to consult her father, but she was not allowed to make promiscuous withdrawals in large amounts. The moneys re-

ceived by each of the children through their withdrawals were used for school allowances, clothing, doctors and hospital bills, and for the other needs of each, except for those withdrawals represented by checks deposited in the taxpayer's individual bank account as above shown. (R. 79.)

The 1936 income and excess profits tax return of the corporation, Birmingham Electric & Manufacturing Company, was subscribed and sworn to by taxpayer as president on March 12, 1937, and filed with the Collector of Internal Revenue for the District of Alabama on March 15, 1937. (R. 79.) On a schedule attached thereto appears the following statement (R. 80):

COMMENT RELATIVE TO DISSOLUTION

> This corporation was dissolved on December 31, 1936, and the net assets were distributed to the stockholder in complete liquidation and cancellation of the capital stock as of that date. The business will be conducted henceforth without interruption by M. M. Argo, as a proprietorship.

Under date of February 23, 1937, taxpayer addressed the following letter to the "Secretary of Treasury, Att: Commissioner of Internal Revenue" (R. 80):

> As provided in Article 308 of Regulation 90 relating to excise tax on employers under Title 9 of Social Security Act, I am hereby giving notice that the Corporation

known as Birmingham Electric & Mfg. Company was dissolved December 31, 1936 and that henceforth the business will be conducted under the same name by M. M. Argo as proprietor.

Annual returns of excise tax under Title IX of the Social Security Act for the years 1937 and 1938 were filed with the same Collector on behalf of the company by taxpayer, who executed the affidavit thereto as "M. M. Argo, Owner." (R. 80.)

Employer's summary information returns under Title VIII of the Social Security Act for the periods January 1 through June 30, 1937, and July 1 through December 31, 1937, were filed with the same Collector on behalf of the company by taxpayer, who executed the affidavit thereto as "M. M. Argo, Owner." (R. 80.)

Seven employer's tax returns under the same title and act were filed with the same Collector quarterly on behalf of the company for the period ended March 31, 1938, through the period ended September 30, 1939, by taxpayer, who executed the affidavit to each as "M. M. Argo, Owner." (R. 80–81.)

Taxpayer filed personal property tax list returns with the tax assessor of Jefferson County, Alabama, covering the personal property of the company, and executed affidavits thereto on December 8, 1937, and October 6, 1938, respectively,

wherein he stated that he was the "owner" of such property. (R. 81.)

Taxpayer, on or about June 10, 1937, filed a financial statement and balance sheet of the company with the First National Bank of Birmingham for credit purposes. The heading, "Corporation," on the printed form was stricken out and the word, "Individual," substituted. The statement showed "condition at close of business April 30th, 1937." The statement was signed in the name of the company, "By M. M. Argo Title of Officer, Owner." On or about March 24, 1939, a balance sheet of the business as of February 28, 1939, was filed by taxpayer with the same bank. It was signed, "M. M. Argo, Owner." (R. 81.)

On December 16, 1940, taxpayer filed a complaint against Henry J. Willingham, the Collector of Internal Revenue for the District of Alabama, in the District Court of the United States for the Southern Division of the Northern District of Alabama, for the recovery of income taxes for the year 1937 alleged to have been paid April 19, 1940, in the amount of $876.14, plus interest, in response to a notice of deficiency determined on the ground that, "there was no bona fide partnership (referring to the Birmingham Electric & Manufacturing Company) and that the net income reported on form 1065 actually represented net income to Mr. M. M. Argo from his individually

conducted business under the name of Birmingham Electric & Manufacturing Company." The complaint further alleged that the business was a partnership during 1937 and that the Commissioner erred in taxing petitioner with all the income of the business. A general denial to this complaint was filed. (R. 81.)

On February 24, 1941, the District Court entered an "Order on Pre-Trial Hearing" wherein it was stated that (R. 82):

> It was agreed by all of the parties that the following are all of the issues in controversy in this cause:
>
> Plaintiff claims refund of income taxes for the year 1937, under the revenue laws of the United States because The Birmingham Electric and Manufacturing Company was a partnership throughout the entire calendar year 1937 and the plaintiff was taxable only on partnership income accruing to him.
>
> Defendant pleads:
>
> (1) The general issue; and
>
> (2) In the taxable year, plaintiff was the individual owner of the said business and was taxable on the entire income therefrom and there was no partnership.

On October 16, 1942, an order of the Court was entered as follows (R. 82–83):

> This cause coming on to be heard prior to the submission of the cause to the jury, the parties stipulated by their respective

counsel, in open Court, that if the jury found from the evidence that there was a partnership between the plaintiff and his wife, and three children during the calendar year 1937 that judgment should be rendered upon such verdict in favor of the plaintiff for the sum of $985.31, plus interest thereon at six per cent per annum from and after April 19, 1940, until paid as provided by law, and that on the other hand, if the jury found from the evidence that no such partnership existed during the calendar year 1937, then judgment should be rendered upon such verdict in favor of the defendant, and the case thereupon being submitted to the jury, the jury reported a verdict as follows:

"We, the jury, find that there was a partnership during the year 1937.

"C. L. COLLINS,
"Foreman."

it is accordingly by the Court

Ordered, Adjudged, and Decreed that the plaintiff herein have and recover of and from the defendant herein the sum of Nine Hundred Eighty-five and 31/100 ($985.31) Dollars, * * *

An appeal from this judgment of the District Court was taken by Henry J. Willingham, Collector, defendant in the suit, to the United States Circuit Court of Appeals for the Fifth Circuit, and on motion filed by the appellant the appeal was dismissed. (R. 83.)

The taxpayer's petition before the Tax Court covering the years 1938 and 1939, was filed February 21, 1942. The petition covering the year 1940 was filed on August 24, 1942. (R. 83.) Before the Tax Court the taxpayer pleaded the judgment against the Collector as *res judicata.* (R. 83.)

The Tax Court held that the judgment of the District Court against the Collector was not *res judicata* in the present proceeding against the Commissioner, and that the partnership was not required to be recognized for tax purposes for the years 1938, 1939, and 1940. (R. 88, 90.) The court below affirmed the decision of the Tax Court. (R. 162–165.)

ARGUMENT

1. The decision below is plainly correct under well established principles of tax law. As taxpayer concedes (Br. 32–33), the judgment of the District Court in favor of taxpayer and against the *Collector* for the recovery of income taxes for 1937 is not *res judicata* in the proceeding against the *Commissioner* wherein the latter refused to recognize the partnership for tax purposes for 1938 and 1939. *Bankers Coal Co.* v. *Burnet,* 287 U. S. 308; *United States* v. *Nunnally Investment Co.,* 316 U. S. 258.[2]

[2] Section 3772 (d) of the Internal Revenue Code, *supra,* which is a legislative reversal of the doctrine that a judgment in a suit against the Collector is not *res judicata* in a subsequent suit against the Commissioner or the United

Hence the Tax Court was free to make its independent finding from all the evidence, with the judgment of the District Court clearly entitled to no "greater weight" than the other evidence contained in the record. (Cf. Pet. Br. 32–34.) See *Sage* v. *United States*, 250 U. S. 33; *Bankers Coal Co.* v. *Burnet*, *supra*; *United States* v. *Nunnally Investment Co.*, *supra*; cf. *Webre Steib Co.* v. *Commissioner*, 324 U. S. 164.

Moreover, there is no necessity for review by this Court of the holding by the courts below as to the inapplicability of the doctrine of *res judicata* to the tax year 1940 since there is unanimity of opinion among the Circuit Courts of Appeal that the doctrine does not apply to the type of problem involved herein where events which determine tax liability are not identical from year to year.[8] Thus, if the

States, does not apply since the petition for redetermination of the deficiencies for 1938 and 1939 was filed before June 15, 1942, its effective date. (R. 83.) However, the section does apply to the controversy for 1940, since the petition for redetermination for that year was filed after June 15, 1942. (R. 83.)

[8] As distinguished from the situation where the question in issue is identical with that decided in the earlier case although involving a different tax year, and arises out of the same facts and historical events which appeared in the record of the former decision. For example, the doctrine of *res judicata* has been held to apply where the questions were whether the bond discount amortized was on the taxpayer's own bonds (*Tait* v. *Western Md. Ry. Co.*, 289 U. S. 620), whether the taxpayer or his children were the owners of certain shares of the family corporation on which the dividends were issued (*Montgomery* v. *Thomas*, 146 F. (2d) 76

question is whether the taxpayer is doing business during the taxable year (*Stoddard* v. *Commissioner,* 141 F. (2d) 76 (C. C. A. 2d)), is selling its product to a subsidiary in an arm's-length transaction (*Campana Corp.* v. *Harrison,* 135 F. (2d) 334 (C. C. A. 7th)), is a social or business club; *Engineers' Club of Philadelphia* v. *United States,* 42 F. Supp. 182 (C. Cls.), Certiorari denied, 316 U. S. 700), or is a manufacturer (*Henricksen* v. *Seward,* 135 F. (2d) 986 (C. C. A. 9th); *Monteith Bros. Co.* v. *United States,* 142 F. (2d) 139 (C. C. A. 7th)), since each year involves similar but not identical factual patterns, the answer must be given in light of the facts of the current year and not by reference to the preceding judgment. Hence where, as here, the problem is not solely the construction of a written or perhaps oral partnership agreement, the conclusion that a partnership exists for tax purposes must depend in each year upon an appraisal of the actual activities and interrelations of the alleged partners and the doctrine of *res judicata* cannot apply.

The case of *Leininger* v. *Commissioner,* 86 F. (2d) 791 (C. C. A. 6th), advanced by taxpayer (Br. 18), is not in conflict with the instant case. There, although the judgment of this Court in

---

(C. C. A. 5th)), or whether the taxpayer was a transferee (*Commissioner* v. *Western Union Tel. Co.*, 141 F. (2d) 774 (C. C. A. 2d)). But see *Pelham Hall Co.* v. *Hassett*, 147 F. (2d) 63 (C. C. A. 1st); *Commissioner* v. *Netcher*, 143 F. (2d) 484 (C. C. A. 7th), certiorari denied, 323 U. S. 759.

Burnet v. *Leininger,* 285 U. S. 136, was held to be *res judicata* as to the husband and wife partnership for later years, the court was careful to say that the new facts sought to be introduced occurred before and affected the husband's status for the tax years in the case decided by this Court and that the husband had no competent evidence to indicate any change in his status for the subsequent tax years. Contrary to taxpayer's assertion (Br. 31), the Commissioner did contend in the court below that (Government's brief, p. 21) there were differences in 1937 and 1940 with respect to the operation of the so-called partnership and the activities and interrelations of taxpayer and his family. In any event, since the issue here involved is not the existence of the partnership in 1937 but in 1940, the court below was correct in holding that in order to work an estoppel by judgment, taxpayer had to show, but did not, that the facts upon which the earlier judgment was based were identical with those arising in 1940. *Russell* v. *Place,* 94 U. S. 606; *Leicht* v. *Commissioner,* 137 F. (2d) 433 (C. C. A. 8th).

2. The decision below presents no occasion for this Court to define further the application of the "substantial evidence" rule to review of decisions of the Tax Court (cf. Pet. Br. 34–37). *Dobson* v. *Commissioner,* 320 U. S. 489, rehearing denied, 321 U. S. 231. For, the court below correctly affirmed the judgment of the Tax Court, either

upon the ground that the facts amply supported the judgment, or upon the ground that income is legally attributable for tax purposes to the person who earned it or whose property produced it. *Helvering* v. *Horst,* 311 U. S. 112; *Helvering* v. *Eubank,* 311 U. S. 122; *Lucas* v. *Earl,* 281 U. S. 111; *Harrison* v. *Schaffner,* 312 U. S. 579; cf. *Griffiths* v. *Commissioner,* 308 U. S. 355; *Commissioner* v. *Court Holding Co.,* 324 U. S. 331. With evidence that taxpayer alone supplied the technical knowledge necessary for the conduct of the business and that the profits during the tax years in question were wholly disproportionate to the capital utilized and invested in the business, the Tax Court surely could not properly be charged with error in finding, or the Circuit Court of Appeals in affirming, that taxpayer was taxable as the real earner of the income. *Lucas* v. *Earl, supra.*

Although this Court is to consider the problem of the family partnership as a device for tax avoidance (see *Commissioner* v. *Tower,* No. 317, this Term, certiorari granted, October 8, 1945, and *Lusthaus* v. *Commissioner,* No. 263, this Term, certiorari granted October 8, 1945), we think the instant case presents merely a familiar instance of an effort to make an anticipatory assignment of income ineffective to relieve the real earner from tax thereon and does not reveal any additional phase of the family partnership problem which should be before this

Court. There is no more reason for further review in this case than in *Doll* v. *Commissioner,* No. 138, this Term, where the Court denied certiorari on the same day that it granted the petitions for certiorari in the *Tower* and *Lusthaus* cases.

CONCLUSION

The decision below is correct; there is no occasion for further review of the issues involved. The petition should therefore be denied.

Respectfully submitted.

J. HOWARD MCGRATH,
Solicitor General.
SAMUEL O. CLARK, JR.,
Assistant Attorney General.
SEWALL KEY,
ROBERT N. ANDERSON,
LEONARD SARNER,
Special Assistants to the Attorney General.

OCTOBER 1945.

U. S. GOVERNMENT PRINTING OFFICE: 1945